

2021 Ads P&L Outlook - V8

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Please see below the latest 2021 Ads P&L outlook (*including organic Search and YouTube*). We expect a total Ads operating profit of [REDACTED] for FY 21, +52% YoY (26% 2Y CAGR), with a 50.5% operating profit margin. Compared to Plan, operating profit is ~\$17.5B higher, reflecting stronger-than-expected revenue momentum across products and meaningful FX benefits. Compared to the previous forecast (referred to as "V7" below), operating profit is \$98M lower, driven by a reduction in YT revenue forecast. **Search+ includes Consumer Gmail but excludes Play Ads.*

- **Summary:** expected growth rates for 2021 are: served rev of **37% YoY** (23% 2Y CAGR); booked rev of **40% YoY** (23% 2Y CAGR); net revenue of **40% YoY** (22% 2Y CAGR); gross margin of **43% YoY** (23% 2Y CAGR); opex of **19% YoY** (14% 2Y CAGR); operating profit of **52% YoY** (26% 2Y CAGR).
- **Served Revenue (fixed-FX):** FY outlook at [REDACTED], **\$21.7B higher than Plan (111.6% Plan attainment)**, and \$0.3B lower than V7. Search and Display outlook were largely unchanged, while YT outlook was \$0.3B lower than V7, driven by a pullback in both A&C (an extension of softness in July) and DR (recent slowdown in top advertisers).
- **Booked Revenue:** FY outlook at [REDACTED], **\$23.6B higher than Plan** driven by the stronger-than-expected served revenue outlook, as well as a **\$3.0B FX gain** due to year-to-date USD weakness. Compared to V7, booked revenue is \$0.3B lower, driven by served revenue forecast reduction.
- **Net Revenue:** FY outlook at [REDACTED], (down \$0.1B vs V7) with 69.6% net revenue margin, **1ppt higher than Plan**, driven by favorable mix including AdMob outperformance within DVA and mix shift to non-CACable formats in YT (Masthead, YT Search). Compared to V7, net revenue margin % is flat.
- **Gross Margin:** FY outlook at [REDACTED], 64.6% gross margin, \$0.3B lower than V7 driven by net revenue reduction and increase in DST forecast. Machine/Network cost is largely unchanged from V7 and \$72M lower than plan driven by savings in Gmail, offset by YouTube unfavorability. Other CoS Y/Y growth is skewed higher due to an accounting change that reclassified \$0.8B digital service tax (DST) from G&A Opex to Other CoS. DST (\$0.2B over plan) and credit card fees (due to rev outperformance) are the primary driver of Other COS unfavorability to budget.
- **Opex:** overall growing **19% YoY**, slower than net revenue and gross margin growth. Compared to plan, we are seeing underspend across EngPM (\$0.9B), more than offset by overspend in G&A (driven by \$0.9B legal settlement, offset by \$0.2B lower than

expected bad debt expense) and TI (represented by price variance, which indicates less materialized savings vs budget). Google Ads Opex is growing 8% YoY, with payroll spend tracking below plan. GBO Opex allocated to Ads P&L is forecasted to grow 20% YoY, roughly in line with plan. Compared to V7, Opex overall is \$0.2B lower, primarily driven by reduction in EngPM payroll/non payroll forecast.

- **Operating profit:** █████ for Total Ads, 50.5% operating profit margin, 4ppt higher YoY. By product, Search+ operating profit outlook is at █████ (65.5% margin), Display at █████ (11.0% margin), and Core YT is █████ (14.7% margin).

Exhibit 1. Total Ads profit contribution

Ads P&L \$ In Billions	Total Ads				
	V8	FY20	vs. Plan	% YoY	2Y CAGR
Served Revenue (Fixed FX)	██████████	██████████	21.7B	37%	23%
Booked Revenue			23.6B	40%	23%
TAC			4.7B	37%	22%
CAC			0.9B	47%	37%
Net Revenue			18B	40%	22%
Other COS			0.3B	71%	41%
Machine/Network			-0.1B	-7%	3%
Gross Margin			17.8B	43%	23%
Gross Margin %			64.6%	63.1%	1.4ppt
			1.5ppt	-0.1ppt	
Total Opex	████	████	0.3B	19%	14%
Opex % Rev.	14.1%	16.6%	-1.7ppt	-2.5ppt	-1.2ppt
EngPM	██████████	██████████	-0.9B	14%	14%
Google Ads			-0.3B	8%	14%
Commerce			0B	24%	5%
Other EngPM			-0.5B	16%	16%
GBO			0B	20%	12%
Marketing	██████████	██████████	0.1B	47%	18%
G&A			0.7B	15%	14%
TI			0.4B	47%	N/A
Operating Profit	██████████	██████████	17.5B	52%	26%
Operating Profit %	50.5%	46.5%	3.1ppt	4ppt	1.15ppt

Exhibit 2. Ads profit contribution broken out by Search+, DVA, YT Ads

Ads P&L \$ In Billions	Search+			DVA			YouTube			Total Ads		
	VB	% YoY	2Y CAGR	VB	% YoY	2Y CAGR	VB	% YoY	2Y CAGR	VB	% YoY	2Y CAGR
Served Revenue (Fbnet FX)		37%	21%	31.2B	36%	22%	29.4B	44%	38%	209	37%	23%
Booked Revenue		40%	21%	27.6B	36%	22%	29.6B	46%	38%	200.7B	40%	23%
TAC		39%	23%	19B	35%	21%				44.8B	37%	22%
CAC		149%	74%				15.9B	46%	37%	16.3B	47%	37%
Net Revenue		40%	20%	6.6B	40%	23%	13.4B	44%	40%	109.6B	40%	23%
Other COS		76%	45%	0.3B	61%	20%	0.4B	54%	43%	3B	71%	41%
Machine/Network		-4%	5%	1.1B	-13%	1%	1.7B	-8%	-1%	6.9B	-7%	3%
Gross Margin		42%	21%	2.2B	64%	29%	11.6B	57%	51%	129.7B	43%	23%
Gross Margin %	77.3%	1ppt	-0.2ppt	26%	2.9ppt	1.35ppt	39%	3ppt	3.2ppt	64.6%	1.5ppt	-0.1ppt
Total Opex		21%	14%	4.1B	7%	9%	7.2B	22%	17%	28.3B	19%	14%
Opex % Rev.		-1.8ppt	-0.7ppt	15%	-4.1ppt	-1.85ppt	24.3%	-4.6ppt	-4.95ppt	14.1%	-2.5ppt	-1.2ppt
EngPM		15%	15%	1.4B	-9%	0%	3.6B	23%	21%	12B	14%	14%
Google Ads		26%	25%	1.2B	-10%	1%	0.6B	10%	19%	3.4B	8%	14%
Commerce		24%	5%							0.9B	24%	5%
Other EngPM		11%	14%	0.2B	-1%	0%	3B	26%	21%	7.8B	16%	16%
GBQ		21%	15%	1.4B	14%	6%	1.3B	21%	12%	6.4B	20%	12%
Marketing		39%	13%	0B	43%	17%	0.8B	73%	37%	2.7B	47%	18%
G&A		19%	14%	1.1B	19%	30%	1.3B	3%	5%	6.1B	15%	14%
TI		70%	N/A	0.2B	20%	N/A	0.3B	31%	N/A	1.1B	47%	N/A
Operating Profit		44%	22%	3B	280%	89%	4.3B	197%		101.4B	52%	26%
Operating Profit %	65.5%	2.8ppt	0.55ppt	11%	7ppt	3.2ppt	14.7%	7.5ppt	8.15ppt	50.5%	4ppt	1.15ppt

Notes:

- 1) Search+ includes Search Ads - PA, and Search - PA. Consumer Gmail is also included in Search+. YT subscription products and Play Ads are excluded.
- 2) The large gap between Search served and booked revenues is due to Play Ads being included in Served Rev (to align with rev reporting elsewhere) but not in Booked Rev.
- 3) Starting FY21, GA is split into Search Ads/DVA on a 67/33 basis - this is the main driver for the fast Google Ads Opex growth in Search+ and the negative Google Ads Opex Y/Y growth in DVA.
- 4) Fast Commerce growth is due to inclusion of Lens costs in Search Ads PA mid-way last year.
- 5) The TI cost definition for Resource Economy vs non-RE has evolved overtime. In particular, Core Systems RE allocations to PA are now considered part of Machine/Network cost, but embedded within non-RE TI cost pre-2020. As a result, 2Y CAGR for TI Opex is marked as N/A.